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VIA ELECTRONIC FILING

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
445 12th Street, SW, Room TWB-204
Washington, DC 20554

Re: *Application by Verizon New England Inc., et. al. To Provide In-Region, InterLATA Services In Vermont, CC Docket No. 02-7.*

Dear Mr. Caton:

Yesterday, I filed this *ex parte* in the aforementioned docket, inadvertently indicating that it was being filed at the request of the Commission Staff. I notified the Bureau of the error and note that this filing should count against AT&T's *ex parte* page limit. This letter submits a corrected *ex parte* notice. AT&T submits this *ex parte* letter in response to the issues raised by Verizon in its March 1, 2002 Reply Comments and its March 18 *ex parte* letter.[1] As demonstrated below, Verizon's latest efforts to fill the critical gaps in its checklist item two showing are plainly inadequate. Verizon has neither met its own burden to demonstrate with record evidence that its Vermont switching and DUF rates are appropriately cost-based nor rebutted the overwhelming evidence that those rates are substantially inflated by numerous TELRIC errors.

I. VERIZON'S RATES CANNOT BE PRESUMED TELRIC-COMPLIANT.

AT&T and other commenters have demonstrated that Verizon's Vermont non-loop rates are infected with numerous TELRIC errors that substantially inflated those rates. In its *March 18 Letter* Verizon again urges the Commission to ignore this evidence and simply presume that Verizon's rates are TELRIC-compliant. According to Verizon, a presumption of TELRIC-compliance is warranted here because the Vermont Public Service Board ("VPSB") approved its inflated non-loop rates. *See id.* Verizon also urges the Commission to adopt a

[1] *See Ex Parte* Letter from Richard T. Ellis (Verizon) to William Caton (Acting FCC Secretary), CC Docket No. 02-07 (March 18, 2002) ("*March 18 Letter*").

presumption of TELRIC-compliance based on the sum of its loop and non-loop rates. Verizon's claims are inconsistent with the record evidence, the 1996 Act, and Commission precedent.

The VPSB had no possible basis to find that Verizon's rates were TELRIC-compliant as of 1997, much less as of today. As explained by the Vermont Hearing Officer, Verizon's "SCIS model [used to compute switching rates] is proprietary and, therefore, cannot be 'opened up' for examination by regulators and competitors." *VPSB Feb. 4, 2000 Order* at 23. Without looking behind Verizon's switching cost assertions, the VPSB had no ability to verify Verizon's claims that its proprietary cost studies complied with TELRIC principles. Thus, even if it were appropriate for the Commission to defer where a state commission *has* rigorously examined the applicant's cost studies and found them TELRIC compliant, that could not be done here – the VPSB by its own admission has never even examined substantial portions of Verizon's cost studies.

Nor is there any record basis for the Commission itself to verify Verizon's claims of TELRIC compliance. As explained in the Supplemental Declaration of Catherine Pitts, *See Ex Parte* Letter from Amy Alvarez (AT&T) to William Caton (Acting FCC Secretary), CC Docket No. 02-07 (March 15, 2002) ("AT&T March 15 Letter"), Verizon has refused to submit either its switch investment cost model or the inputs to that model. Both are critical to assessing whether Verizon's switching rates are TELRIC-compliant. *See id.* ¶ 4. Verizon has also failed to explain or, in any way document, the methodology used to convert the output of the SCIS model (estimates of switching investment) into the relevant switching port and usage costs. *See id*. ¶ 5. Without this information, the Commission cannot determine independently whether Verizon's non-loop rates were developed consistent with TELRIC principles.

In its Application, Verizon asserted that its Vermont loop and non-loop rates were nonetheless entitled to a presumption of TELRIC-compliance because each of those rates were similar to the rates that were in place in New York at the time Verizon filed its application. However, less than two weeks after Verizon filed its Application, the New York state commission substantially reduced Verizon's New York rates. Verizon's Vermont non-loop rates now exceed those in New York by more than 100 percent. *See* Lieberman Decl. ¶ 17. And that rate difference is not remotely explained by cost differences. According to the Commissions Synthesis Cost Model, Verizon's Vermont non-loop costs are only 57 percent higher than those in New York. *See id.*

Verizon does not deny these facts. Instead, Verizon invites the Commission to ignore them – and Commission precedent – and "benchmark" the sum of Verizon's Vermont loop and non-loop rates to the sum of its loop and non-loop rates in other states. The Commission has never approved a section 271 application on the basis of such a "kitchen sink" comparison, and for good reason. A BOC's rates for a network element comply with sections 251 and 252 (and hence Checklist Item 2) only if they are "based on the cost . . . of providing . . . *the* network element." 47 U.S.C § 252(d)(1) (emphasis added). Thus, the plain language of the Act confirms that to gain Section 271 approval the BOC bears the burden of proving that the rates for each of its network elements complies with TELRIC principles. The whole purpose of unbundling is to allow an entrant to purchase – at cost-based rates – only the elements necessary to implement its particular entry strategy. If a BOC were free to evade the requirement to offer each element that qualifies for unbundling at cost-based rates by offering some elements at low rates and others at inflated rates, the BOC would have the ability to tailor its rates to impede the entry strategies that posed the greatest risk to its local monopolies. Moreover, CLECs are not indifferent to the level of non-loop and loop costs. A substantial portion of non-loop costs are recovered on a usage basis, whereas loop costs are fixed. A CLEC that serves high usage customers, therefore, would be very sensitive to usage costs, and less sensitive to non-usage costs.[2]

To be sure, the Commission has recognized that the potential arbitrariness of certain allocations may require some combination of rate elements to achieve meaningful comparisons. The Commission has, for example, compared total switching costs (and even total non-loop costs) in recognition of the fact that states may differ in the ways that they allocate such costs among usage and port charges. However, no such issues arise with non-loop and loop-related costs. That is because the Commission's rules specifically prohibit state commissions from allowing carriers to allocate loop-related costs to a switching element or vice-versa. *See* 47 U.S.C. 51.509(a)-(b). *See also PA 271 Order* ¶ 66 ("we consider the reasonableness of loop and non-loop rates separately"); *KA/OK 271 Order* ¶¶ 82-95 (comparing loop costs only); *MA 271* ¶ 26 (comparing only non-loop rates).

Where, as here, the applicant's non-loop rates are higher (on a cost-adjusted basis) than those in a valid benchmark state, the applicant must prove – with specific cost evidence – that its non-loop rates are appropriately cost-based. Verizon did not, and could not, do that.

II. VERIZON'S VERMONT RATES ARE INFLATED BY MYRIAD TELRIC VIOLATIONS.

Because it has so clearly failed to demonstrate that its Vermont switching rates are cost-based, Verizon struggles to avoid Commission scrutiny of those rates, claiming that AT&T's failure to "ask the [VPSC] . . . to reconsider the rate . . . or initiate a proceeding to revisit the rate" bars the Commission from questioning Verizon's unsupported claims of TELRIC compliance. To the contrary, Section 271 makes clear that it is the applicant's obligation to prove its claims of checklist compliance; that it is the Commission's obligation to critically analyze the applicant's claims; and that neither obligation turns on the strengths or weaknesses of third parties' showings in other fora.[3] Where, as here, a BOC fails to demonstrate compliance with Checklist Item Two, its application must be denied. The contrary ruling that Verizon seeks could not survive judicial review.

In this case, despite the limited access to Verizon's Vermont cost studies – both in the state proceeding and in this proceeding – AT&T and other commenters have identified numerous obvious TELRIC-errors that inflate Verizon's non-loop rates. The Commission cannot, as Verizon urges, simply ignore these serious errors or Verizon's complete failure to meet its Checklist Item Two burden.

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[2] Verizon's claim that no CLEC *currently* purchases switching elements separately from loop elements is beside the point. If Verizon were permitted to charge above-cost rates for certain elements simply because they were not purchased separately today, that would enable Verizon to foreclose all future entry strategies that rely on purchasing those elements separately.

[3] *See, e.g., Kansas/Oklahoma 271 Order* ¶ 29 ("the BOC applicant retains at all times the ultimate burden of proof that its application satisfies all of the requirements of section 271, even if no party files comments challenging its compliance with a particular requirement"); *New York 271 Order* ¶ 49 (the BOC applicant must make "a *prima facie* case that it meets the requirements of a particular checklist item" and "must plead, with appropriate supporting evidence, facts which, if true, are sufficient to establish that the requirements of section 271 have been met").

DUF Rates. Verizon now concedes that its DUF rates are computed "using regionwide data" and that its New York DUF rates "were developed using essentially the same methodology." *VZ March* 18 Letter at 5. Therefore, Verizon's Vermont DUF rates should not substantially differ from its New York DUF rates. Yet, Verizon's Vermont DUF rates result in monthly per line DUF charges that are *seven times higher* than those in New York. *See* Lieberman Decl. ¶ 30.

Verizon frankly admits that the reason its Vermont DUF rates are so much higher in Vermont than in New York is that its New York rates are based on "additional information [that] is now available based on experience since the rates were initially set" in 1996. Today's DUF rates, Verizon concedes, should be lower (as they are in New York) because "the estimate of the amount of time required to process a CLEC's request for usage information is now shorter, resulting in lower costs." *VZ March 18 Letter* at 5.[4] Thus, even according to Verizon, its Vermont DUF rates are not cost-based.

Verizon contends, however, that the Commission should ignore the fact that Verizon's DUF rates are not TELRIC-compliant because, Verizon says, a Section 271 proceeding is not an appropriate context to raise such claims. That is obviously wrong. As explained above, Checklist Item Two requires BOCs to prove that their UNEs are TELRIC-compliant today. Here, Verizon has not only failed to meet its burden of proving that its rates comply with TELRIC principles, but has actually conceded that its DUF rates do not comply with Checklist Item Two.

Verizon's citation to the D.C. Circuit's decision in the New York proceeding and to the *RI 271 Order* are inapposite. The D.C. Circuit decision held only that some deference may be due the Commission's Section 271 decisions. *See AT&T* v. *FCC,* 220 F.3d 607, 631 (D.C. Cir. 2000). And, in the *RI 271 Order*, the Commission simply explained that "[t]he fact that the Rhode Island Commission has scheduled a rate proceeding to update existing rates does not, *in itself*, prove that existing rates are not TELRIC compliant." *RI 271 Order* ¶ 31 (emphasis added). The situation here is entirely different. Here, the claim is not that Verizon's rates should be rejected because they are being reviewed by the VPSB, rather the claim is that Verizon has *admitted*, and commenters have demonstrated, that Verizon's Vermont DUF rates are inflated by non-TELRIC assumptions. On this record, there can be no non-arbitrary finding that Verizon's DUF rates satisfy Checklist Item Two.

Switch Discounts. The VPSB ordered Verizon to compute its Vermont rates based on the switch prices that reflect the switch discounts received by Verizon when purchasing new switches. Because Verizon has not made its cost models available for inspection, it is impossible to verify Verizon's bald assertion that it complied with this mandate. *See Feb. 4 2000 Order* at 27 ("the TELRIC methodology rightly assumes that the efficient prices for unbundled elements are those necessary to cover the costs of a newly deployed network, it follows that the fully discounted costs of new switches be modeled. I cannot tell if they were").

[4] There are also other TELRIC errors that inflate Verizon's DUF rates. DUF rates are highly sensitive to usage forecasts. Higher usage forecasts allow DUF costs to be spread over more orders (resulting in lower per unit rates), and lower usage forecasts mean that DUF costs must be spread fewer orders (resulting in higher per unit costs). Because usage has increased substantially since 1996, Verizon's 1996 DUF usage is substantially lower than today's usage, further contributing to Verizon's overstated Vermont DUF rates.

However, as explained in the Declaration of Catherine Pitts (attached to AT&T's initial comments), based on the limited information that Verizon has made available and the sheer magnitude of Verizon's Vermont switch rates, it should be clear that Verizon has not, in fact, computed its Vermont switch rates based on switch costs that reflect new switch discounts.

A comparison of Verizon's Vermont switch costs to those in New York illustrates this point. Unlike the VPSB, the New York Commission allowed Verizon to compute switch costs partially based on the cost of switches that reflect growth (as opposed to new) switches. Because growth switch discounts are less than new switch discounts, it would be expected that Verizon's Vermont switch costs would be lower than those in New York on a cost-adjusted basis. But that is not the case. Verizon's Vermont fully installed switch investment ($274) are nearly 66 percent higher than those ordered in New York ($165) even though the Commission's Synthesis Cost Model confirms that Verizon's Vermont switch investment exceeds that in New York by only about 34 percent. *See* Lieberman Decl., Exhibit A-7. This discrepancy strongly suggests that Verizon's Vermont switch costs do not reflect new switch discounts.

Another indication that Verizon's Vermont cost model does not reflect switch discounts is that Verizon has conceded that in other states it pays only $69 to $88 per line for new Nortel switches. *See* Pitts Decl. ¶ 18. Although Verizon purportedly uses only Lucent switches in Vermont, there is no valid reason for Lucent switches to cost twice as much as Nortel switches. In fact, Verizon frankly concedes that Lucent and Nortel switches should be competitively priced "because Lucent knows that it is competing with Nortel and Siemens for Verizon's business." *VZ March 18 Letter* at 4.

Verizon's only response is that it is reasonable for Verizon to have chosen Lucent switches over Nortel switches because Lucent switches are more appropriate for rural states than are Nortel switches. *See VZ March 18 Letter* at 3. That claim is rebutted by Verizon's own witness who has testified that Lucent and Nortel switches are "functionally interchangeable."[5] In any event, Verizon misses the point. The issue here is not which brand of switches Verizon should have deployed in its network but, rather, whether Verizon's switch costs (for Lucent switches) are forward-looking and cost-based. The fact that Verizon's switch costs for the Lucent switches in its Vermont cost model are twice those of Nortel switches suggests that Verizon's Vermont switch cost inputs are substantially inflated.

Busy Hour Assumptions. Verizon concedes that it recovers its "total" switching costs in Vermont over weekday usage that takes place on only 251 days of the year. *See VZ March 18 Letter* at 6. That means that Verizon's cost study assumes that *no* calls take place on

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[5] Massachusetts UNE Rate Proceeding, Docket No. D.T.E. 01-20 (January 24, 2002) (Question: "Is it fair to say that Lucent 5ESS switches and Nortel DMS 100 switches are functionally interchangeable?"; Answer: "Are they functional substitutes for one another as local-exchange switches? Yes."); *See also id.* (Verizon witness explaining that Lucent and Nortel switches, "if they want to be competitive . . . have to be substitutes for one another"). Moreover, the only purported difference between Lucent and Nortel switches identified by Verizon is that Lucent switches "can trunk calls directly from remotes," whereas Nortel switches cannot. *VZ March 18 Letter* at 3. But the limited cost data that Verizon has put in the record in this proceeding show that Verizon does not actually trunk calls from remotes in Vermont. *See* Verizon-Vermont Workpaper, Part B, pp. 77-81 (showing inputs for 30 remote switches and none has a trunk). Thus, this purported difference between Lucent and Nortel switches, is not relevant in Vermont.

holidays or on weekends. And that means that Verizon's rates guarantee massive windfalls and are not remotely cost-based. *All* CLEC weekend/holiday traffic – nearly a third of the year – is pure "gravy" over and above Verizon's actual forward-looking switching costs, which are designed to be recovered in full through business day traffic.

The New York state commission has already identified this ploy and rejected it. The New York commission recognized that it would be unreasonable for Verizon to compute rates that assume away all weekend and holiday calling.[6] However, the New York Commission determined that, for New York, weekend calling volumes were typically less than business day calling volumes. *See id.* Accordingly, the New York commission required Verizon to count each weekend day as one-half of a weekday. *See id.* Thus, Verizon recalculated its switching costs by spreading its switch investment over 308 days (business days plus ½ weekend days), rather than over 251 days.

In Vermont, Verizon should spread its switch investment costs over all 365 days of the year. Verizon has made no showing that weekend and holiday call volumes in Vermont are any lower than weekend volumes. And given the rural nature of Vermont and the increased call volumes related to Internet traffic, Verizon's weekend call volumes are unlikely to differ substantially from business day volumes. Because Verizon failed to account for the entire year when computing switching costs, Verizon's per minute switching rates are inflated by 31 percent.

Installation Factor. Verizon's installation factors are substantially inflated above TELRIC levels. *See* Pitts Decl. ¶¶ 20-22. Verizon now concedes that its installation factors are based on Verizon's Vermont Detailed Continuing Property Record ("DCPR") database from 1995. *March 18 Letter* at 4. That is, Verizon's installation factors are based on the costs of its embedded network in 1995. Verizon's 1995 installation costs could not possibly have been TELRIC-compliant for 1997, and clearly would not be TELRIC-compliant today. Verizon does not even attempt to justify its substantially overstated installation factors. Instead, Verizon once again asserts that no party has sought reconsideration or review of those factors and, therefore, should not be allowed to challenge them here. As explained above, that argument lacks merit and must be rejected.

Sincerely,

Robert W. Quinn, Jr.

cc:	Dorothy Attwood	Julie Saulnier
	Deena Shetler	Julie Veach
	Tamara Preiss	Ann Berkowitz (Vz)
	Gary Remondino	

[6] *See* Order on Unbundled Network Element Rates, *Proceeding on Motion of the Commission to Examine New York Telephone Company's Rates for Unbundled Network Elements*, Case 98-1357, at 36-39 (January 28, 2002).